



Thrift Savings Plan

FUND

INFORMATION

July 2005

We're glad you asked . . .

. . . about your TSP investment options. The information in this booklet will help you decide how to invest your account.

To get started, first determine your approach to investing. You can manage your own account or put your money in one of the “lifecycle funds” — L Funds—that are invested according to a professionally determined mix of the G, F, C, S, and I Funds based on various time horizons.

If you decide to invest your entire account in one of the L Funds, you're done making decisions. The TSP will do the rest.

If you choose your own investment mix from the G, F, C, S, and I Funds, remember that the amount you contribute and your investment allocation are the most important factors affecting the growth of your TSP account. As you read the fund descriptions, think about these points:

- ✓ **Consider both risk and return.** The F Fund (bonds) and the C, S, and I Funds (stocks) have higher potential returns than the G Fund (Government securities). But stocks and bonds also carry the risk of investment losses that the G Fund does not. On the other hand, investing entirely in the G Fund may not give you the returns you need to meet your retirement savings goal.
- ✓ **You need to be comfortable with the amount of risk you expect to take.** Your investment comfort zone should allow you to use a “buy and hold” strategy so that you are not chasing market returns during upswings, or abandoning your investment strategy during downswings.
- ✓ **You can reduce your overall risk by diversifying your account.** The five individual TSP funds offer a broad range of investment options, including Government securities, bonds, and domestic and foreign stocks. Generally, it's best not to put all of your eggs in one basket.
- ✓ **The amount of risk you can sustain depends upon your investment time horizon.** The more time you have before you need to withdraw your account, the more risk you can take. (This is because early losses can be offset by later gains.) As your time horizon shortens, you may need to modify your investment mix.
- ✓ **Periodically review your investment choices.** Check the distribution of your account balance among the funds to make sure that the mix you chose is still appropriate for your situation. If not, rebalance your account to get the allocation you want.

For more information about TSP investment options, visit the Web site, **www.tsp.gov**. You can get recent and historical rates of return, use the calculators to estimate the effect of various rates of return on your account balance, and read TSP *Highlights* articles about investing.

Remember, there is no guarantee that future rates of return will match historical rates.



L FUNDS

Lifecycle Funds

Fund Information

Inception

August 1, 2005

Administrative Expense Ratio

Based on administrative expenses of the G, F, C, S, and I Funds in proportion to their allocations in the L Funds.

In 2004, expenses were approximately \$0.60 per \$1,000 account balance.

Investment Objective

Fund	Growth	Preservation of Assets
L 2040	High	Very Low
L 2030	High	Low
L 2020	Moderate/High	Low
L 2010	Moderate	Moderate
L Income	Low	High

Time Horizons

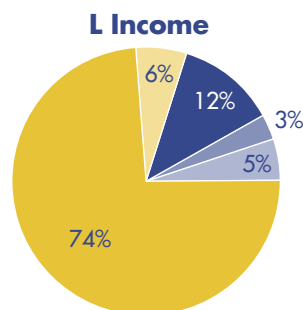
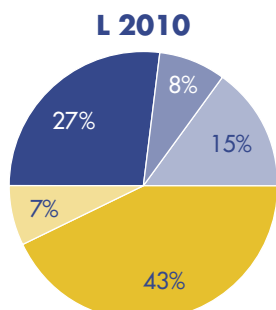
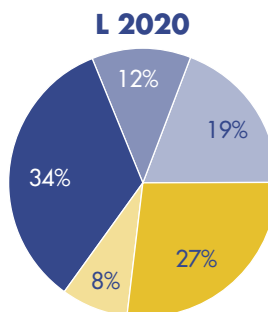
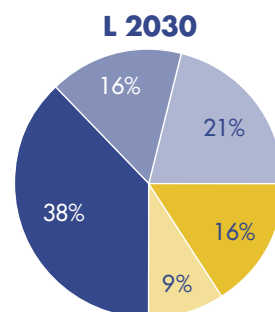
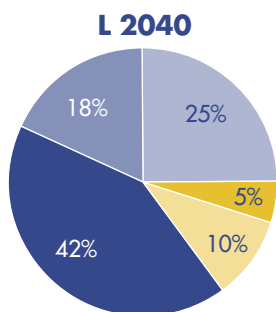
(when you expect to need the money)

Choose:	If your time horizon is:
L 2040	2035 or later
L 2030	2025 through 2034
L 2020	2015 through 2024
L 2010	2008 through 2014
L Income	Sooner than 2008

Key Features

- The L Funds diversify participant accounts among the G, F, C, S, and I Funds, using professionally determined investment mixes (allocations) that are tailored to different time horizons. The L Funds are re-balanced to their target allocations each business day. The investment mix of each fund adjusts quarterly to more conservative investments as the fund's time horizon shortens.
- The objective of the L Funds is to provide the highest possible rate of return for the amount of risk taken.
- Investing in the L Funds is not a guarantee against loss and does not eliminate risk. The L Funds are subject to the risks inherent in the underlying funds, and can have periods of gain and loss.
- The L Funds' expected returns will be approximately equal to the weighted average of the G, F, C, S, and I Funds' returns. Earnings will be calculated daily and there will be a daily share price for each L Fund.

Initial Asset Allocations



G Fund F Fund C Fund S Fund I Fund

L FUND FACTS

The L Funds are intended to meet the investment needs of TSP participants with time horizons that fall into five different date ranges, as shown on the front. The five L Funds were designed for the TSP by Mercer Investment Consulting, Inc. The asset allocations are based on Mercer's economic assumptions regarding future investment returns, inflation, economic growth, and interest rates. Mercer will review these assumptions at least annually and determine whether changes to the allocations are warranted.

L 2040, L 2030, L 2020, and L 2010 are for participants with time horizons that fall within the defined date ranges. The asset allocations of these funds are adjusted quarterly, moving to a more conservative mix, gradually approaching those of the L Income Fund. Between quarterly adjustments, the asset allocations of each fund are maintained through daily rebalancing to that fund's target allocation. When a fund reaches its horizon, it will roll into the L Income Fund, and a new fund will be added with a more distant horizon. For example, in 2010 when the L 2010 Fund rolls into the L Income Fund, a new L 2050 Fund will be created.

The L Income Fund is designed to produce current income for participants who are already receiving money from their accounts through monthly payments, and for participants who plan to withdraw or begin withdrawing their account before 2008. The asset allocation of the L Income Fund does not change over time; it is maintained through daily rebalancing.

The pie charts on the front show the initial allocations of the L Income, L 2010, L 2020, L 2030, and L 2040 Funds in each of the five underlying TSP funds. The allocation in the G Fund, which has the least amount of risk, is largest in the L Income Fund, and becomes successively smaller with the more distant target dates. In contrast, the allocations in the F, C, S, and I Funds, which carry varying amounts of risk, but also the potential for higher returns, are largest in L 2040 and smallest in the L Income Fund.

The graph below depicts the expected return and risk associated with each of the five L Funds at inception. The expected returns are derived from Mercer's economic assumptions and are not guaranteed. Expected variability of the investment returns is a measure of risk in investing. For each risk level, there is one "optimal" asset allocation that provides the highest expected return. The collection of optimal asset allocations make up the "Efficient Frontier," which is shown by the curve. Asset allocations that are below the Efficient Frontier are less than optimal, because there is an asset allocation along the frontier that provides a higher return for the same level of risk, or lower risk for the actual returns received.

The five TSP L Funds have initial asset allocations that correspond to points shown on the Efficient Frontier. Putting your entire TSP account into one of the L Funds allows you to achieve the best expected return for the amount of expected risk.

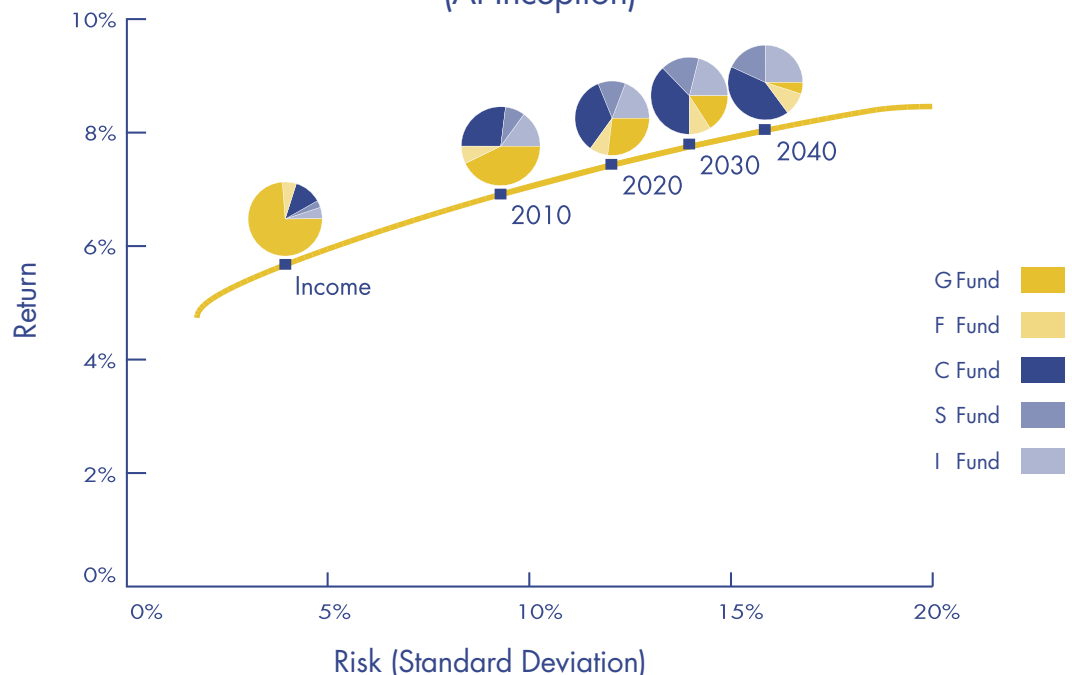
Over time, the L Funds (except for the Income Fund) will "roll down" the efficient frontier. That means that, as their allocations are adjusted each quarter, the funds shift left on the line, becoming less risky, until they eventually merge into the L Income Fund.

The administrative expenses associated with the L Funds are those of the underlying G, F, C, S, and I Funds, calculated in proportion to their allocations in each L Fund. The L Funds do not have any additional charges. There are no restrictions on investing in the L Funds. You may invest any part of your TSP account in any L Fund,

and even invest in more than one L Fund. But it is recommended that you put your entire TSP account into just one L Fund—the one with the target date that is closest to your time horizon. Any other strategy may result in an asset allocation that is less than optimal (i.e., not on the Efficient Frontier), or which is not suited to your investment time horizon.

Remember, however, that risk and expected return are based on assumptions about future economic conditions and investment performance. There is no guaranteed rate of return for any period, either short-term or long-term.

L Funds and the Efficient Frontier (At Inception)





G FUND

Government Securities Investment Fund

Fund Information

Net Assets

as of December 31, 2004
\$58.8 billion

2004 Administrative Expense Ratio

.06% (6 basis points)
\$0.60 per \$1,000
account balance

Asset Manager

Federal Retirement
Thrift Investment Board

Returns

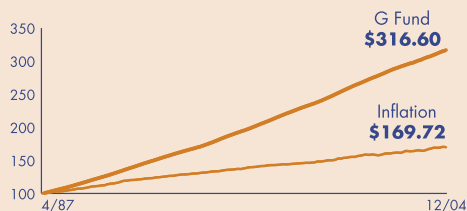
as of December 31, 2004

	G Fund ¹	G Fund-Related Securities ²
1 Year	4.3	4.4
5 Year	5.0	5.0
10 Year	5.7	5.8
Since Inception April 1, 1987	6.7	6.8

¹After expenses ²Without deductions

Growth of \$100

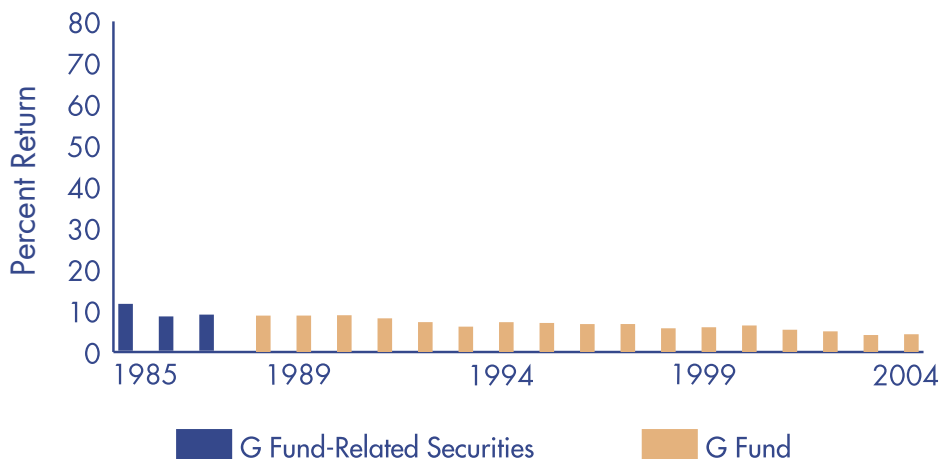
Since Inception



Key Features

- The G Fund offers the opportunity to earn rates of interest similar to those of long-term Government securities but without any risk of loss of principal and very little volatility of earnings.
- The objective of the G Fund is to maintain a higher return than inflation without exposing the fund to risk of default or changes in market prices.
- The G Fund is invested in short-term U.S. Treasury securities specially issued to the TSP. Payment of principal and interest is guaranteed by the U.S. Government. Thus, there is no "credit risk."
- Earnings consist entirely of interest income on the securities.
- Interest on G Fund securities has outpaced inflation and 90-day T-bills.

G Fund Returns* 1985–2004



* For periods before the inception of the G Fund, the rate shown is the statutory rate (without deduction for administrative expenses).

G FUND FACTS

By law, the G Fund must be invested in nonmarketable U.S. Treasury securities specially issued to the TSP. The G Fund investments are kept by electronic entries which do not involve any transaction costs to the TSP. The G Fund rate is set once a month by the U.S. Treasury based on a statutorily prescribed formula (described below), and all G Fund investments earn that interest rate for the month. (The G Fund rate is also used in other Government programs, such as the Social Security and Medicare trust funds and the Civil Service Retirement and Disability Fund.)

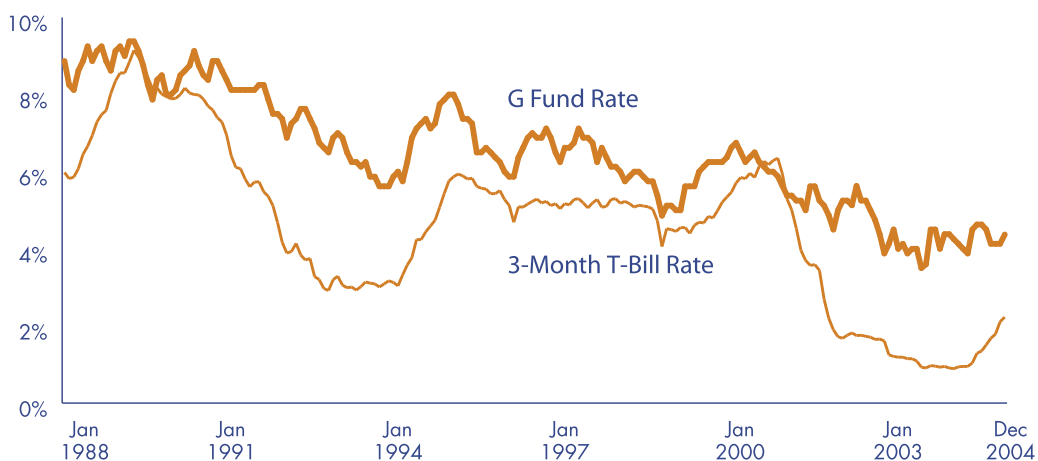
The Board invests the G Fund exclusively in short-term securities (with maturities ranging from 1 day to 4 days over holiday weekends), but the securities earn a long-term interest rate. Because the Federal Retirement Thrift Investment Board pursues its strategy of investing the G Fund in short-term securities, the value of G Fund securities does not fluctuate; only the interest rate changes. Thus, when the monthly G Fund interest rate goes up, G Fund earnings accrue faster; when the G Fund interest rate declines, G Fund earnings accrue more slowly.

Calculation of G Fund Rate—G Fund securities earn a statutory interest rate equal to the average market yield on outstanding marketable U.S. Treasury securities with 4 or more years to maturity. The G Fund rate is calculated by the U.S.

Treasury as the weighted average yield of approximately 70 U.S. Treasury securities on the last day of the previous month. The yield of each security has a weight in the G Fund rate calculation based on the market value of that security. (Market value is the outstanding dollar amount of the security measured at its current market price. The larger the dollar amount of a security outstanding, the larger its weight in the calculation.) The Treasury securities used in the G Fund rate calculation have a weighted average maturity of approximately 12 years.

G Fund Yield Advantage

January 1988–December 2004



The annualized G Fund interest rate averaged 1.9 percentage points (187 basis points) more than 3-month T-bill rates since January 1988.

The G Fund Yield Advantage—The G Fund rate calculation described above, along with the Board's policy of investing exclusively in short-term maturities, results in a long-term rate being earned on short-term securities. Because long-term interest rates are generally higher than short-term rates, G Fund securities usually earn a higher rate of return than do short-term marketable Treasury securities. In the chart above, the G Fund rate is compared with the rate of return on 3-month marketable Treasury securities (T-bills). From January 1988 through December 2004, the G Fund rate was, on average, 1.9 percentage points higher per year than the 3-month T-bill rate.



F FUND

Fixed Income Index Investment Fund

Fund Information

Net Assets

as of December 31, 2004
\$10.1 billion

2004 Administrative Expense Ratio

.05% (5 basis points)
\$0.50 per \$1,000
account balance

Number of Securities

3889

Average Duration

4.3 years

Average Coupon Rate

5.25%

Benchmark Index

Lehman Brothers U.S. Aggregate
bond index
www.lehman.com

Asset Manager

Barclays Global Investors

Returns

as of December 31, 2004

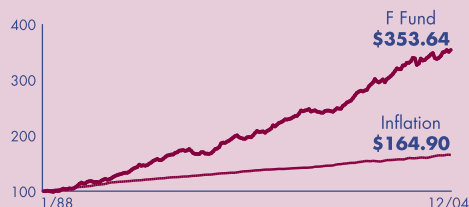
	F Fund ¹	LBA Index ²
1 Year	4.3	4.3
5 Year	7.7	7.7
10 Year	7.7	7.7
Since Inception	7.7	8.1

Jan. 29, 1988

¹After expenses ²Without deductions

Growth of \$100

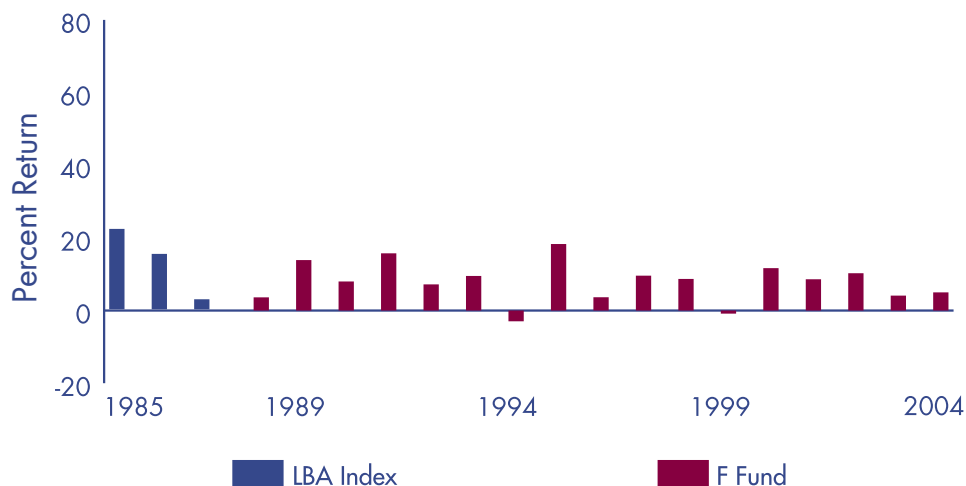
Since Inception



Key Features

- The F Fund offers the opportunity to earn rates of return that exceed those of money market funds over the long term (particularly during periods of declining interest rates), with relatively low risk.
- The objective of the F Fund is to match the performance of the Lehman Brothers U.S. Aggregate (LBA) index, a broad index representing the U.S. bond market.
- The risk of nonpayment of interest or principal (credit risk) is relatively low because the fund includes only investment-grade securities and is broadly diversified. However, the F Fund has market risk (the risk that the value of the underlying securities will decline) and prepayment risk (the risk that the security will be repaid before it matures).
- Earnings consist of interest income on the securities and gains (or losses) in the value of securities resulting from changing market interest rates.

F Fund Returns* 1985-2004



* For periods before the inception of the F Fund, the rate shown is the return of the LBA index (without deduction for management fees, trading costs, and administrative expenses).

F FUND FACTS

By law, the F Fund must be invested in fixed-income securities. The Federal Retirement Thrift Investment Board has chosen to invest the F Fund in an index fund that tracks the Lehman Brothers U.S. Aggregate (LBA) index, a broadly diversified index of the U.S. bond market.

The **LBA index** consists of high quality fixed-income securities with maturities of more than one year. The index represents the U.S. Government, mortgage-backed securities, corporate, and foreign government sectors of the U.S. bond market.

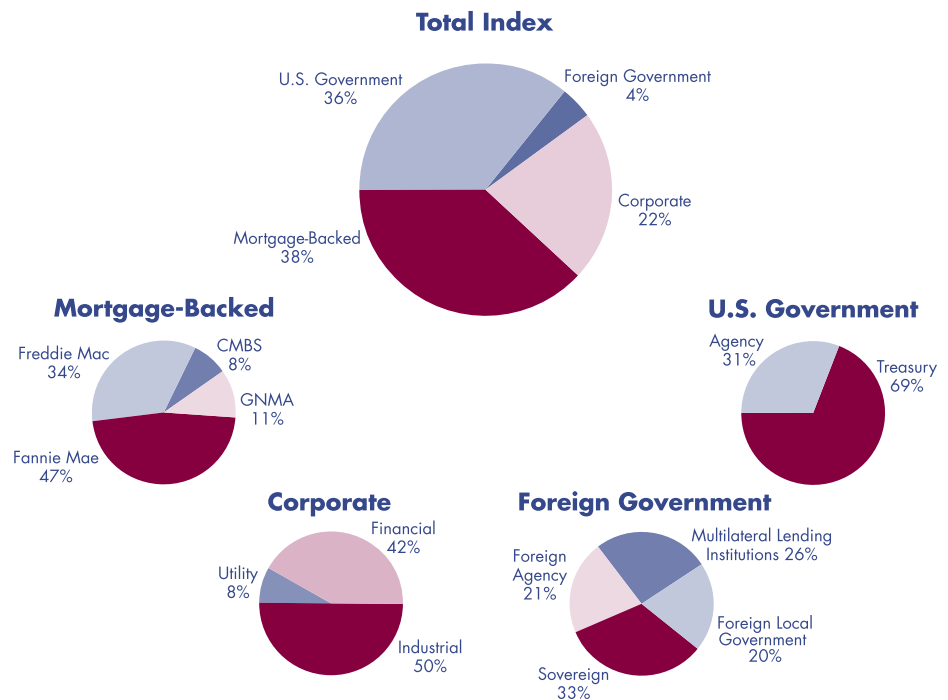
On December 31, 2004, the LBA index included 5,836 notes and bonds. The average LBA index coupon rate was 5.24%, which means that, on an annual basis, interest income equalled approximately 5.24% of the face value of the securities in the LBA index. The average duration of the LBA index was 4.3 years, which means that a 1% increase (decrease) in interest rates could be expected to result in a 4.3% decrease (increase) in the price of the security. New issues are added continuously to the LBA index, and older issues drop out as they reach maturity.

Barclays U.S. Debt Index

Fund—The F Fund is invested in the Barclays U.S. Debt Index Fund. Because the LBA index contains such a large number of securities, it is not feasible for the Barclays U.S. Debt Index Fund to invest in each security in the index. Instead, Barclays selects a representative sample of the various types of mortgage-backed, U.S. Government, corporate, and foreign government securities included in the overall index. Within each sector, Barclays selects securities that, as a whole, are designed to match important index characteristics such as duration, yield, and credit rating. The performance of the U.S. Debt Index Fund is evaluated on the basis of how closely its returns match those of the LBA index.

The F Fund invests in the Barclays U.S. Debt Index Fund by purchasing shares of the Barclays U.S. Debt Index Fund “E,” which in turn holds shares of the Barclays U.S. Debt Index Master Fund. As of December 31, 2004, F Fund holdings constituted \$9.7 billion of the U.S. Debt Index Master Fund, which itself held \$26.3 billion in securities.

LBA Index Bond Market Sectors December 31, 2004





C FUND

Common Stock Index Investment Fund

Fund Information

Net Assets
as of December 31, 2004
\$65.7 billion

2004 Administrative Expense Ratio

.06% (6 basis points)
\$0.60 per \$1,000
account balance

Benchmark Index

Standard & Poor's 500
stock index
www.standardandpoors.com

Asset Manager

Barclays Global Investors

Returns

as of December 31, 2004

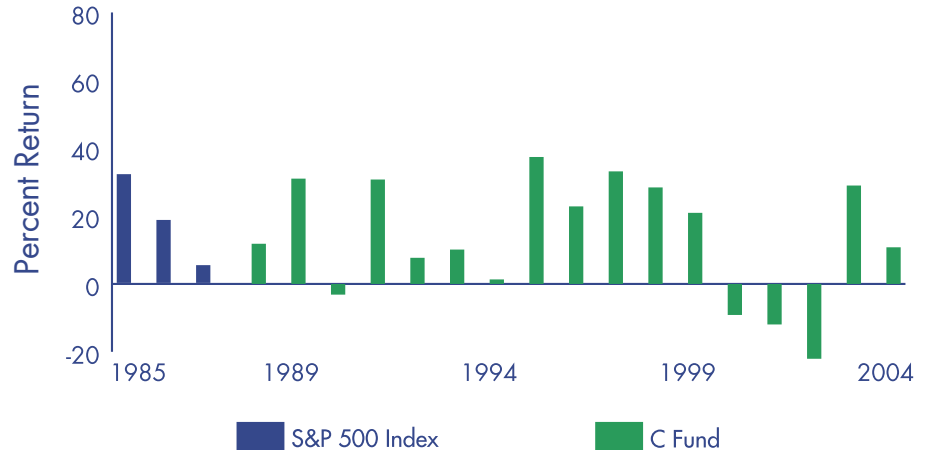
	C Fund ¹	S&P 500 Index ²
1 Year	10.8	10.9
5 Year	-2.3	-2.3
10 Year	12.0	12.1
Since Inception Jan 29, 1988	12.1	12.4

¹After expenses ²Without deductions

Key Features

- The C Fund offers the opportunity to earn a potentially high investment return over the long term from a broadly diversified portfolio of stocks of large and medium-size U.S. companies.
- The objective of the C Fund is to match the performance of the S&P 500 index, a broad market index made up of stocks of 500 large to medium-size U.S. companies.
- There is a risk of loss if the S&P 500 index declines in response to changes in overall economic conditions (market risk).
- Earnings consist of gains and losses in the prices of stocks, and dividend income.

C Fund Returns* 1985-2004



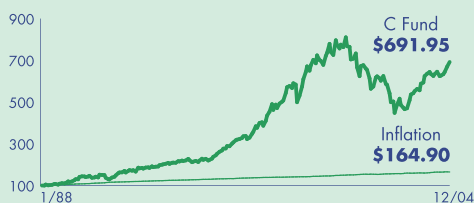
* For periods before the inception of the C Fund, the rate shown is the return of the S&P 500 index (without deduction for management fees, trading costs, or administrative expenses).

S&P 500 Top Ten

Company	Percent of Index
General Electric	3.42
Exxon Mobil Corporation	2.93
Microsoft Corporation	2.57
Citigroup, Inc.	2.22
Wal-Mart Stores, Inc.	1.98
Pfizer, Inc.	1.79
Bank of America Corporation	1.68
Johnson & Johnson	1.67
American International Group	1.52
International Business Machines	1.45

Growth of \$100

Since Inception



C FUND FACTS

By law, the C Fund must be invested in a portfolio designed to replicate the performance of an index that includes stocks representing the U.S. stock market. The Federal Retirement Thrift Investment Board has chosen as its benchmark the S&P 500 index, which tracks the performance of major U.S. companies and industries.

The **S&P 500 index** is an index of 500 large to medium-size U.S. companies that are traded in the U.S. stock markets. The index was designed by Standard & Poor's Corporation (S&P) to provide a representative measure of U.S. stock market performance. As of December 31, 2004, 493 common stocks and 7 real estate investment trusts (REITs) were included in the index. (REITs accounted for 0.6 percent of the index's market value.) The companies in the index represented 113 separate industries classified into the 10 major industry groups shown in the chart. The S&P 500 index made up 78% of the market value of the U.S. stock markets.

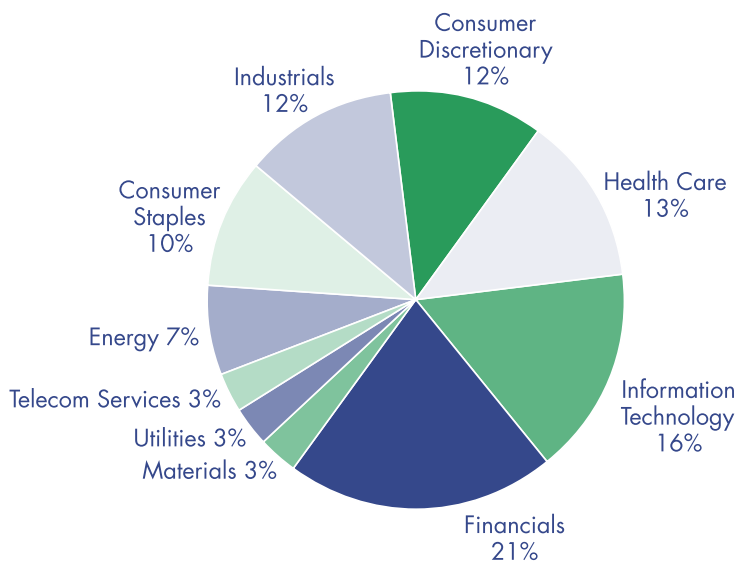
The S&P 500 is considered a "big company" index. As of December 31, 2004, the largest 100 companies in the S&P 500 represented 66% of the index's market value. Currently, the S&P 500 index is weighted by full market capitalization. A company's weighting in the index is the total market value of the company (that is, the share price multiplied by the total number of shares outstanding) as a percentage of the combined market value of all companies in the index. During

2005, the S&P 500 index will move to a float-adjusted market capitalization, in which a company's market value and its weighting in the index are calculated using the number of shares that are freely traded, rather than all outstanding shares. Shares that are not freely traded, such as the holdings of controlling shareholders and their families, company management, and other companies, are excluded from the calculation.

Barclays Equity Index Fund — The C Fund is invested in the Barclays Equity Index Fund. The C Fund holds all the stocks included in the S&P 500 index in virtually the same weights that they have in the index. The performance of the Equity Index Fund is evaluated on the basis of how closely its returns match those of the S&P 500 index. A portion of Equity Index Fund assets is reserved to meet the needs of daily client activity. This liquidity reserve is invested in S&P 500 index futures contracts.

The C Fund invests in the Barclays Equity Index Fund by purchasing shares of the Barclays Equity Index Fund "E," which in turn holds primarily shares of the Barclays Equity Index Master Fund. As of December 31, 2004, C Fund holdings constituted \$63.2 billion of the Equity Index Master Fund, which itself held \$124.0 billion of securities.

S&P 500 Index Major Industry Groups December 31, 2004





S FUND

Small Capitalization Stock Index Investment Fund

Fund Information

Net Assets

as of December 31, 2004
\$10.0 billion

2004 Administrative Expense Ratio

.06% (6 basis points)
\$0.60 per \$1,000
account balance

Benchmark Index

Dow Jones Wilshire 4500 Completion
stock index
www.wilshire.com or
www.djindexes.com

Asset Manager

Barclays Global Investors

Returns

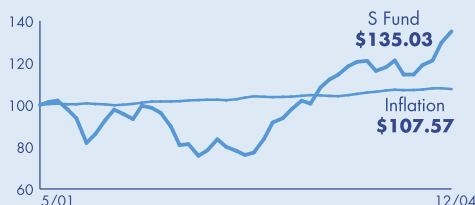
as of December 31, 2004

	S Fund ¹	DJW 4500 Index ²
1 Year	18.0	18.1
5 Year	N/A	1.3
10 Year	N/A	11.9
Since Inception May 1, 2001	8.5	8.8

¹After expenses ²Without deductions

Growth of \$100

Since Inception



Key Features

- The S Fund offers the opportunity to earn a potentially high investment return over the long term by investing in the stocks of small and medium-size U.S. companies.
- The objective of the S Fund is to match the performance of the Dow Jones Wilshire 4500 Completion (DJW 4500) index, a broad market index made up of stocks of U.S. companies not included in the S&P 500 index.
- There is a risk of loss if the DJW 4500 index declines in response to changes in overall economic conditions (market risk).
- Earnings consist of gains and losses in the prices of stocks, and dividend income.

S Fund Returns* 1985–2004



* For periods before the inception of the S Fund, the rate shown is the return of the DJW4500 index (without deduction for management fees, trading costs, or administrative expenses).

DJW 4500 Top Ten

Company

Percent of Index

Berkshire Hathaway, Inc. (Class A stock)	3.08
Liberty Media Corporation (Class A stock)	0.97
Genentech, Inc.	0.86
The DIRECTV Group, Inc.	0.52
IAC InterActiveCorp	0.47
Juniper Networks, Inc.	0.46
Amazon.com, Inc.	0.44
Sirius Satellite Radio, Inc.	0.33
Kraft Foods, Inc. (Class A stock)	0.31
Vornado Realty Trust	0.30

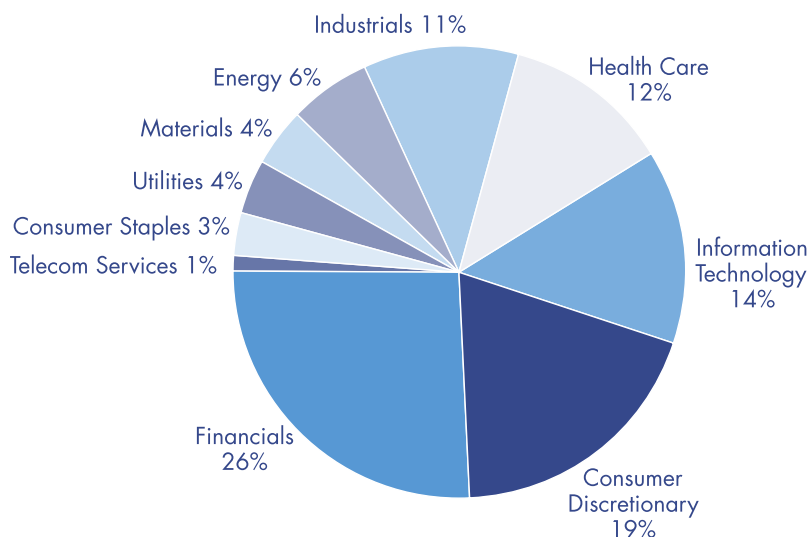
S FUND FACTS

By law, the S Fund must be invested in a portfolio designed to replicate the performance of an index of U.S. common stocks, excluding those that are held in the C Fund. The Federal Retirement Thrift Investment Board has chosen, as its benchmark, the Dow Jones Wilshire 4500 Completion index, which tracks the performance of the actively traded non-S&P 500 stocks in the U.S. stock market.

The **Dow Jones Wilshire 4500 Completion index (DJW 4500 index)** is an index of all actively traded U.S. common stocks and real estate investment trusts (REITs) that are not included in the S&P 500 index. The index is designed to be the broadest measure of the non-S&P 500 domestic stock markets. As of December 31, 2004, the index included 4,493 common stocks and 223 REITs. (REITs accounted for 7.8% of the index's market value.) The DJW 4500 index made up 22% of the market value of the U.S. stock markets; the S&P 500 accounted for the other 78%. Thus, the S Fund and the C Fund combined cover virtually the entire U.S. stock market.

The DJW 4500 index is weighted by float-adjusted market capitalization, in which a company's market value and its weighting in the index are calculated using the number of shares that are freely traded, rather than all outstanding shares. Shares that are not freely traded, such as the holdings of controlling shareholders and their families, company management, and other companies, are excluded from the calculation. A company's weighting in the index is the float-adjusted market value of the company (that is, the share price multiplied by the number of freely traded shares outstanding) as a percentage of the combined float-adjusted market value of all companies in the index. As of December 31, 2004, the largest 100 companies in the DJW 4500 index represented 24% of the index's market value.

DJW 4500 Index
Major Industry Groups
December 31, 2004



Barclays Extended Market Index Fund — The S Fund is invested in the Barclays Extended Market Index Fund. The DJW 4500 index contains a large number of stocks, including illiquid stocks with low trading volume and stocks with prices less than \$1.00 per share. Therefore, it is not practical for the Barclays Extended Market Index Fund to invest in every stock in the index. The Barclays fund holds the stocks of most of the companies in the index with market values greater than \$1 billion. However, a mathematical sampling technique is used to select among the smaller stocks. Barclays' mathematical model considers size and industry group to match the industry weights in the index. Within each industry group, Barclays selects stocks that, together, are expected to produce a return that is very close to the industry's return in the DJW 4500 index. The performance of the Extended Market Index Fund is evaluated on the basis of how closely its returns match those of the DJW 4500 index. A portion of Extended Market Index Fund assets is reserved to meet the needs of daily client activity. This liquidity reserve is invested in futures contracts of the S&P 400 and Russell 2000 (other broad equity indexes).

The S Fund invests in the Barclays Extended Market Index Fund by purchasing shares of the Barclays Extended Market Index Fund "E," which in turn holds primarily shares of the Barclays Extended Market Index Master Fund. As of December 31, 2004, S Fund holdings constituted \$9.6 billion of the Extended Market Index Master Fund, which itself held \$14.8 billion in securities.



I FUND

International Stock Index Investment Fund

Fund Information

Net Assets

as of December 31, 2004
\$7.3 billion

2004 Administrative Expense Ratio

.06% (6 basis points)
\$0.60 per \$1,000
account balance

Benchmark Index

Morgan Stanley Capital
International EAFE
stock index
www.msci.com

Asset Manager

Barclays Global Investors

Returns

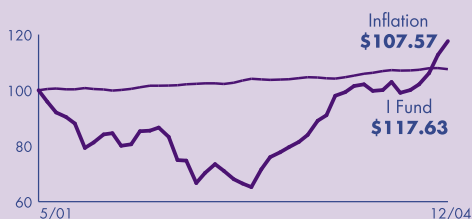
as of December 31, 2004

	I Fund ¹	EAFE Index ²
1 Year	20.0	20.2
5 Year	N/A	-1.1
10 Year	N/A	5.6
Since Inception May 1, 2001	4.5	4.9

¹After Expenses ²Without Deductions

Growth of \$100

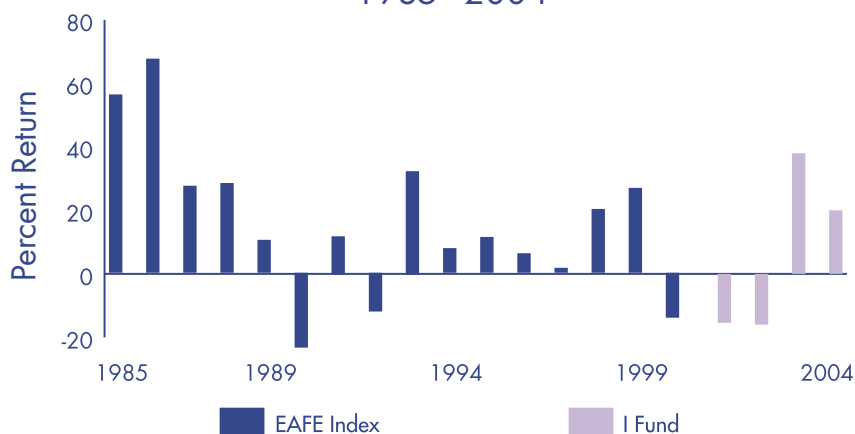
Since Inception



Key Features

- The I Fund offers the opportunity to earn a potentially high investment return over the long term by investing in the stocks of companies in developed countries outside the U.S.
- The objective of the I Fund is to match the performance of the Morgan Stanley Capital International EAFE (Europe, Australasia, Far East) index, a broad international market index, made up of stocks of companies in 21 developed countries.
- There is a risk of loss if the EAFE index declines in response to changes in overall economic conditions (market risk) or in response to increases in the value of the U.S. dollar (currency risk).
- Earnings consist of gains and losses in the prices of stocks, currency changes relative to the U.S. dollar, and dividend income.

I Fund Returns* 1985-2004



* For periods before the inception of the I Fund, the rate shown is the return of the EAFE index (without deduction for management fees, trading costs, or administrative expenses).

EAFE Top Ten

Company	Percent of Index
BP	2.36
HSBC Holdings (GB)	2.08
Vodafone Group	2.00
GlaxoSmithKline	1.54
Total	1.43
Novartis	1.34
Royal Dutch Petroleum Company	1.34
Toyota Motor Corporation	1.31
Nestlé	1.18
Royal Bank of Scotland	1.18

I FUND FACTS

By law, the I Fund must be invested in a portfolio designed to track the performance of an index of common stocks, representing international stock markets outside of the United States. The Federal Retirement Thrift Investment Board has chosen as its benchmark the Morgan Stanley Capital International EAFE (Europe, Australasia, Far East) index, which tracks the overall performance of the major companies and industries in the European, Australian, and Asian stock markets.

A significant component of the returns on the EAFE index (and the I Fund) results from changes in the value of the U.S. dollar relative to the currencies of the countries represented in the index. For example, the EAFE index earned 20.2% in 2004, but part of that return reflected a decline in the value of the U.S. dollar (which increased the return). If the value of the dollar had been unchanged during 2004, the return would have been 12.7%.

The **EAFE index**, designed by Morgan Stanley Capital International (MSCI), is an index of the equity markets of the developed world outside of the United States and Canada. It is the most widely used international stock index. As of December 31, 2004, the index covered the equity markets of 21 countries, as shown in the table.

The companies in the EAFE index are large companies. The index is weighted by float-adjusted market capitalization, in which a company's market value and its weighting in the index are calculated using the number of shares that are freely traded, rather than all outstanding shares. Shares that are not freely traded, such as the holdings of controlling shareholders and their families, company management, and other companies, are excluded from the calculation. Also excluded are shares subject to foreign ownership limitations imposed by governments or companies. Within each country, a company's weighting is the float-adjusted market value of the company (that is, the share price multiplied by the number of freely traded shares outstanding) as a percentage of the combined float-adjusted market value of all companies in the index. Similarly, a country's weighting in the EAFE index is the float-adjusted market value of its stock market as a percentage of the combined float-adjusted market value of all stock markets included in the EAFE index.

Barclays EAFE Index Fund—The Barclays fund holds common stocks of all the companies represented in the EAFE index in virtually the same weights that they have

in the index. The return on the Barclays fund (and on the I Fund) will differ from that of the EAFE index on days when Barclays makes a "fair valuation" adjustment to reprice the securities held by the fund. Fair valuation adjustments are made on days when there are large movements in either U.S. equity markets or exchange rates after the foreign markets have closed. Fair valuation prevents traders from "market timing" by making investment decisions based on "stale" prices, thus diluting the returns of other TSP participants who invest in the I Fund.

The performance of the EAFE index fund is evaluated on the basis of how closely its returns match those of the EAFE index, without the effect of fair valuation. A portion of EAFE Index Fund assets is reserved to meet the needs of daily client activity. This liquidity reserve is invested in futures contracts on the local stock indexes of the countries in the EAFE index. These include the United Kingdom's FTSE 100, Germany's DAX, France's CAC 40, Australia's ALL ORDS, Japan's Nikkei 300, and Hong Kong's Hang Seng.

The I Fund invests in the Barclays EAFE Index Fund by purchasing shares of the Barclays EAFE Index Fund "E," which in turn holds primarily shares of the Barclays EAFE Index Master Fund. As of December 31, 2004, I Fund holdings constituted \$7.0 billion of the EAFE Index Master Fund, which itself held \$42.5 billion of securities.

EAFE Index Country Composition December 31, 2004

Country	Percent of Total Value of Index	Number of Companies
Europe		
Austria	0.4	13
Belgium	1.3	21
Denmark	0.8	20
Finland	1.4	19
France	9.4	57
Germany	7.0	47
Greece	0.6	20
Ireland	0.9	15
Italy	4.3	41
Netherlands	4.8	26
Norway	0.6	14
Portugal	0.4	10
Spain	4.1	32
Sweden	2.5	44
Switzerland	6.8	35
United Kingdom	25.0	152
Europe	70.3	566
Australasia/Far East		
Australia	5.1	71
Hong Kong	1.7	38
Japan	21.9	344
New Zealand	0.2	16
Singapore	0.8	35
Australasia/Far East	29.7	504
Total EAFE Index	100%	1070

Source: Morgan Stanley Capital International

